Special Report

WORLD CIGARETTE SITUATION

NORTH AMERICA

Mexico- The 2002 cigarette production level is forecast to remain unchanged from the previous year because of growing health concerns and cigarette price increases. Cigarette production is estimated at 46.9 billion pieces in 2002. Since Mexico's economic downturn in late 1990s, smokers have shifted from higher priced cigarettes made of high quality flue-cured, burley and oriental tobaccos to mid and low-priced cigarettes made with lower quality flue-cured, light air cured and dark air cured tobaccos.

Mexican cigarette exports in 2002 are forecast at 20 million pieces, unchanged from 2001. Processors report exports of both low priced domestic brands and non-branded cigarette mostly to the U. S. and Eastern European countries.

United States-Smokers consumed an estimated 422 billion cigarettes in 2001, about 2 percent less than the previous year. Price increase, higher taxes, and expanding regulations are the main factors in declining cigarette use. Cigarette exports during 2001 reached 133.9 billion pieces, compared with 147.9 billion the previous year. For 2002, cigarette exports are forecast at 135 billion. Cigarette sales overseas continue to decline because of increased cigarette production by U.S. manufacturers in other countries and a growing health awareness that has dampened cigarette consumption in many markets.

Cigarette output in 2001 decline by almost 3 percent or to 580 billion. The U.S. cigarette industry has stabilized after higher prices and tax increases caused lower production during the past few years. For 2002, cigarette production is expected to remain unchanged from 2001.

CENTRAL AMERICA

Guatemala-There is only one cigarette manufacturer in Guatemala, Tabacalera Centroamericana S.A. (TACASA), a Phillip Morris subsidiary. Tabacalera National S.A. (TANSA), a British American Tobacco subsidiary works as a cigarette distributor from Honduras.

Cigarette production is forecast at 4.2 billion pieces in 2002 compared to 3.9 billion in 2001. This increase is attributed to a slight increase in local cigarette consumption and increased demand from other Central American countries. Cigarette imports are forecast to grow slightly because of increased domestic cigarette demand.

TACASA is expected to export 2.5 million cigarettes in 2002, up nearly 14 percent due to increased demand from other Central American countries.

SOUTH AMERICA

Brazil-Cigarette production for 2002 is estimated at 107 billion pieces, as compared to 109.4 billion pieces in 2001 due to contraband cigarettes from other countries eroding legal sales. Cigarette consumption for 2002 is forecast at 108 billion pieces, compared to 109 billion pieces from the previous year. Contraband cigarettes, especially from Paraguay, which are marketed locally at significantly lower prices, are of major concern for Brazilian cigarette companies because of eroding local sales. Contraband cigarette sales accounted for approximately 34 percent of the actual domestic consumption for 2001.

Brazil is projected to export 500 million pieces of cigarettes in 2002, a 25-percent drop from 2001. The decrease in cigarette exports is a result of a 150 percent export tax which was imposed to prevent cigarette exports to Paraguay and Uruguay from being re-exported to Brazil for tax-free resale.

EUROPEAN UNION

Germany- Cigarette production is expected to continue to grow due to increased demand in Spain and Italy. For 2002, cigarette output is forecast at 218 billion pieces, up 2 percent from 2001. Cigarette exports are estimated to reach a high of 110 billion in 2002 compared to 105.8 billion pieces in 2001.

Domestic demand is projected to grow marginally. High taxes and a price hike have slowed the demand for cigarettes as the German consumer is becoming more price sensitive. The market share of private (discounted) brands grew by 40 percent in 2001 from 2000. Private brands are forecast to capture 15.6 percent of the total cigarette market in 2002.

Italy- Italy's Treasury department announced in June 2002 the sale of their tobacco monopoly, Ente Tabacchi Italiani, ETI. This announcement was not a surprise to the tobacco industry since ETI formed a manufacturing agreement with Philip Morris last January. This 3-year manufacturing agreement replaces their former license contract. ETI officials announced last spring that this agreement represents ETI first step towards privatization.

Italian cigarette production in 2002 is forecast at 45.8 billion pieces compare to 44.7 billion in 2001. Domestic brands are losing market share to foreign brands. Since 1999, domestic brands have lost about 4 percent of the market whereas foreign brands have expanded market share to about 10 percent. However, the market share of foreign brands is actually larger than officially reported because of sales of smuggled cigarettes.

Netherlands- The Dutch cigarette industry is the largest in Europe. Total cigarette production in 2002 is projected to decrease by 2 percent to 120 billion pieces from 2001.

The Netherlands is a transshipment location for cigarettes going to European markets such as France and Italy. Cigarette imports are projected to increase by nearly 60 percent in 2002. A majority of these imported cigarettes will be distributed throughout the European Union. This 60 percent increase is attributed to lower domestic cigarette production and higher domestic consumption. Cigarettes are mainly imported from other EU member states and the United States.

Spain: Cigarette sales continue to climb and are expected to reach a record level in 2002. Much of this growth is on account of a strong tourist market along with lower retail price compared to other European countries. Cigarette sales are estimated to reach 94 billion pieces in 2002.

United Kingdom- Cigarette production is estimated to total 126 billion pieces in 2002 unchanged from 2001. Cigarette consumption of duty paid cigarettes is forecast to continue to decline due to the ongoing high tax policy (about 84 percent of retail value) and to anti-smoking campaigns in the UK. Smokers in the UK are switching from premium to middle-priced brands. Major companies have reacted to consumer demand for cheaper cigarettes by launching their own economy brands. Nearly all of the UKs' cigarette imports come from other EU countries. In addition to legal cigarette imports, it is estimated that around 28 billion cigarettes entered the country as personal or illegal imports in 2001. Unrecorded cigarette imports are projected on the rise. Legal cigarette imports are forecast to increase by 3 percent in 2002 from the previous year.

Currently, there are 15 million adult smokers representing about 30 percent of the adult population in the country. The United Kingdom is a significant cigarette exporter and relies totally on leaf tobacco imports with over half of the cigarettes produced being exported. Although cigarette production is forecast to remain unchanged in 2002, cigarette manufacturers are holding large stocks of cigarettes in case of unanticipated demand. Cigarette exports are forecast at 102 billion pieces, up slightly from the previous year. Some in the industry are expecting that the export market will rebound due to the economic recovery in the Far Eastern markets and the competitive Sterling compared to the U.S. dollar. Important markets for U.K. cigarettes are Germany, Spain, Singapore, Hong Kong, South Korea, and Saudi Arabia

EASTERN EUROPE

Croatia- Croatia's only cigarette producing company, Tvornica Duhana Rovinj, is expected to increase production by 5 percent in 2002. Cigarette production reached 14 million pieces in 2001 and is expected to reach 14.7 million in 2002. Although domestic cigarette consumption is forecast to drop 19 percent, nearly 15 percent of cigarette sales are thought to come from the black market. Thus, true cigarette sales are hard to gauge.

Cigarette exports to ex Yugoslavia countries are expected to increase by 41 percent in 2002 from the previous year.

Poland- Increasing anti-smoking campaigns and illegal cigarette imports have attributed to a decline in cigarette production. In 2002 cigarette production is forecast at 76.5 billion pieces, down 8 percent from 2001.

Russia- 2002 will be the third consecutive difficult year for the tobacco industry because of a continuing surplus of cigarettes and intensifying competition according to industry sources. Cigarette and papirosas (a type of Russian cigarette) production is forecast at 375 billion pieces in 2002, up slightly from a year ago. As a result of overproduction and high import taxes, cigarette imports are forecast to decline by almost 30 percent in 2002. Most western brand cigarettes are produced in Russia in order to avoid the high import tax. Cigarette sales to Kazakhstan, Mongolia, Central Asia, and CIS countries are expected to increase by 56 percent in 2002

Turkey-Turkey continues to be a large cigarette consuming country. To meet domestic and export demand, manufacturers have increased their production capacity and invested in new plants. In addition, consumer preference is slowly switching from an oriental cigarette to a blended cigarette. For 2002, cigarette production is forecast at 128.7 billion pieces, up only marginally from 2001. However, an economic downturn and growing health concerns have adversely affected cigarette consumption. Cigarette consumption is expected to remain stagnant in 2002.

Turkey is becoming a significant cigarette exporter due to its location and low cost of production. Cigarette exports are forecast to increase by 3 percent in 2002. Major markets for Turkish cigarettes are the Gulf States and neighboring Middle Eastern countries.

ASIA

China-The Chinese tobacco industry is restructuring in order to remain competitive in the domestic and overseas markets. Consumer incomes are rising, and they are demanding a higher quality cigarette. Sources report that manufacturers are unable to keep with up the demand for high quality cigarettes. The State Tobacco Monopoly Association is focused on improving cigarette quality. The government is encouraging consolidation and elimination of the least efficient and lowest quality manufacturers. The Chinese government implemented a new taxation system based on quantity and price. In short, small manufacturers will be levied higher taxes. Cigarettes valued under $6 per cartoon will be taxed 30 percent of retail sale and an additional $18.1 per case. It is likely that small scale and low quality cigarette manufacturers will be eliminated due to this new tax structure.

Cigarette production reached 1.70 trillion pieces in 2001, up 2.2 percent from 2000. For 2002, cigarette production is estimated to reach 1.70 trillion, unchanged from 2001. Cigarette exports for 2001 amounted to 13.8 billion, up 7.8 percent over 2000. Exports are likely to increase due to increased sales abroad. Major markets for Chinese were the United States, Hong Kong, Mexico and Central America.

Cigarette imports in 2002 are likely to reach 1.877 billion pieces, up 5 percent from 2001. This 5 percent increase is due to lower tariffs. China is scheduled to drop tariffs from 65 percent in 2001 to 35 percent in 2002. The United Kingdom is the largest exporter of cigarettes to China, with a market share of 52 percent in 2001. The United Sates ranked as the second largest exporter with a market share of 13.6 percent in 2001.

Hong Kong- Hong Kong smokers are becoming more price conscious because of a sluggish economy. Sources report that most Hong Kong smokers prefer American type cigarettes but many are opting for lower priced brands.

Hong Kong is not a significant cigarette producer but serve as a transshipment location to other Asian markets. Total cigarette imports (including smuggled) in 2002 are estimated to increase slightly to 21.5 million as compared to 21.1 million pieces a year earlier. Major suppliers of cigarettes were the United Kingdom, China, and the United States. Cigarette exports are forecast to increase to 29.1 million in 2002 as compared to 27.8 million pieces in 2001. Vietnam, China, Philippines, and Turkey were major re-export markets.

Malaysia- Cigarette production is estimated at 31.3 billion pieces in 2002, up 10 percent from a year ago due to anticipated demand in both the domestic and overseas markets. In addition, international manufacturers are producing brand name cigarettes in Malaysia because of high import tariffs for these products. Domestic consumption is expected to increase by 8 percent because of an improved economic situation.

Cigarette exports in 2002 are expected to rebound reaching 10 billion pieces as compared to 9 billion in 2001. Potential markets for Malaysian cigarettes are Belgium, Hong Kong, and Singapore.

India- India’s cigarette production is forecast to recover marginally to 91.5 billion pieces in 2002. High cigarette prices lowered the production of cigarettes to an estimated 86.3 million pieces last year. Because of the price hike consumers shifted from brand named cigarettes to the mini-cigarette sector. A popular mini-cigarette in India is Beedi.

Cigarette exports are expected to jump 16 percent in 2002 to 1.1 billion pieces. The increase can be attributed to a rebound in the Middle East, Singapore, and in the former Soviet states.

Japan- Cigarette production is forecast up slightly to 241 billion cigarettes. Domestic consumption is estimated to increase marginally despite growing anti-smoking campaigns. Japan’s total cigarette imports are forecast up slightly in 2002. For 2001, cigarette imports dropped 1.6 percent from 83,478 million pieces in 2000 to 82,125 million. Foreign imports accounted for a 25.7 percent market share in 2001 as compared to 25.1 percent in 2000. The U.S. share of imports declined 2.0 percent in 2001 from the previous year.

Japan is one of the world's top cigarette exporters. Japanese cigarette exports were 21 billion pieces in 2001, up 47 percent from the previous year. Principal export destinations were Taiwan, South Korea, and Singapore.

Korea-The Korean tobacco monopoly, Korea Tobacco & Ginseng Corporation (KTGC), will be abolished by end of 2002. The Korean government plans to sell their 33 percent stake in the corporation this year. KTGC is offering tax incentives and introducing new cigarette brands in order to attract foreign investment. British American Tobacco is the only direct foreign investor in the Korean tobacco sector.

The domestic cigarette market is forecast to contract marginally due to increased competition from cheaper foreign brands and from the growing anti-smoking campaign. Foreign cigarette brands currently control a record 20 percent of the cigarette market. Cigarette use is expected to decline by 5 percent, but this figure may be inaccurate given that consumers stockpiled cigarettes prior to the February 2001 cigarette tax hike. Cigarette production in 2002 is expected to drop by nearly 5 percent or to total 93 billion pieces from the previous year. Cigarette imports are expected up by 29 percent.

KTGC's long-term strategy is to increase exports as a percent of total manufactured volume. Currently, KTGC is forecast to export 20 percent of cigarettes produced. By 2005, KTGC goal is to export 30 percent of production. KTGC sees export markets as key to its long-term financial well being as the domestic market becomes more competitive. For 2002, cigarette exports are forecast at 18 billion pieces, up approximately 41 percent from 2001.

AFRICA AND THE MIDDLE EAST

South Africa- Cigarette production and use is slowing due to increased taxes and strict labeling requirements. Cigarette production is expected to reach 27.5 billion pieces in 2002, down 2 percent from the previous year. Stricter anti-tobacco legislation was passed last year, which limited advertising and restricted smoking areas. The tar yield of cigarettes must not be greater than 12 mg per cigarette and nicotine yield not greater than 1.2 mg by June 1, 2006. Cigarette imports from the U.S. are declining as more U.S. cigarettes are produced locally, opening the door for expanded U.S. leaf tobacco exports.